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SUBJECT: SWEDEN ASKS ABOUT U.S. EXPECTATIONS FOR THE G-20 SUMMIT;  
DISCUSSES ECONOMIC SITUATION IN LATVIA AND SWEDEN

¶1. (SBU) Summary: As EU President, Sweden has asked what sort of political success the U.S. is seeking from the G-20 Summit in Pittsburgh. State Secretary for Finance Per Jansson noted the need to show concrete progress in handling the financial crisis, and on climate change. He also discussed economic developments in Latvia, where he sees mixed progress; and in Sweden where slight signs of recovery are starting to show. End Summary.

Expectations for the G-20 Summit?  
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¶2. (SBU) In an August 21 meeting with DCM, Finance Ministry State Secretary Per Jansson noted that everybody wants the Pittsburgh G-20 Summit to be a success, and as the party representing the European position, Sweden would like to understand the U.S. view of what sort of political success (e.g. deliverables) we will be looking for from the Summit. Since it will not be enough to confirm that we will deliver on the London commitments, he asked, what are the U.S. thoughts on what Pittsburgh will actually deliver?

¶3. (SBU) Jansson thought G20 progress on climate has been "very good" because it is one of the few places where developing and developed countries can discuss climate change. He said his government is interested in the U.S. view on what it would take to call this a success, will having a good discussion be sufficient, are we looking for deliverables?

¶4. (SBU) Jansson asked what were U.S. expectations for discussion at the G20 about IMF restructuring, noting that there were internal discussions at the IMF. (Comment: Sweden is concerned about the Nordic seat at the IMF. The U.S. has told Swedish officials that consolidation of the IMF Board needs to happen, but how Europe consolidates is a matter for Europe to sort out. End Comment.)

Latvia  
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¶5. (SBU) On the Baltics, Jansson thought things were better than a month ago when we had a "really bad situation" because the gap between the EU and IMF positions sent bad signals. He noted that the joint team visiting Riga concluded that the Latvian government had done a lot on spending, and little on income, leaving a 15% gap, which doesn't work. He said the Latvian government would do a little on taxes, with some concrete revenue enhancers in the spring of 2010, but it would not amount to much. He thought it good that the government set the contours of the 2010 budget, and noted that if the spending reforms fail, the government would consider VAT and income tax reform. Jansson said the Latvia package would go to the Board on August 27. He thought the Board was already OK with it, but the IMF staff had problems.

¶6. (SBU) Jansson stressed that the underlying problems in Latvia remained, although the current account was now in a surplus. The country needed adjustment now, so the crisis does not happen again. He described the currency as weak but fragile, and that defense of

it had cost 6% of GDP. He noted that the debate over whether the government would/should devalue had pushed the currency lower as people safeguarded themselves against devaluation.

¶17. (SBU) Jansson described the danger of contagion if the situation in Latvia gets worse, noting that Lithuania would not be able to keep its exchange rate, and wondering how robust Estonia would be. He wondered what would happen to the other 8 floating exchange rate countries in the region, e.g. Poland and Bulgaria. Problems there would create pressure on the eurozone, and feedback to Sweden and other Western countries.

#### It's Good to Be Out of the Eurozone

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¶18. (SBU) This led Jansson to convey his perspective on the value to Sweden of being out of the eurozone at the present time. He noted that Finland's GDP had fallen 11% in the second quarter, while Sweden with a similar export mix had its GDP fall only 5% (currently). He concluded that the 6% extra drop was in the exchange rate. He noted that many in Sweden are talking about moving to the euro in the midst of the economic crisis for stability, but it is stability at a low level.

¶19. (SBU) Jansson said that Sweden and the IMF had worked up the plan for the IMF to publicly say that the Swedish krona was undervalued. He said that in the long-run the Swedish government does not want the currency undervalued, and is not doing anything active in the market to affect the exchange rate. He expected some nominal depreciation of the exchange rate as it returns to equilibrium.

#### Planning for the Unlikely Worst-Case Scenario

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¶10. (SBU) Jansson reviewed Sweden's contingency planning for a worst case scenario, describing the legislation in place that allows the government to nationalize banks. He said the government would take over banks and separate good and bad assets afterwards rather than buying impaired assets first because "valuation is hopeless." The toughness of the restructuring conditions imposed on a bank would depend on the level of government intervention required. If a bank were able to raise 70percent private capital, the government would help with very loose conditions. If the bank was able to remain private, but needed more government capital, it would face tough conditions. The third tier would be banks actually taken over by the government. He stressed that Sweden never plans to have to use these tools, but the threat of government take over motivates banks to avoid problems. He cited the example of the recent rights offering by Swedbank where a relatively small amount of government support garnered criticism for the banks leadership.

¶11. (SBU) Jansson illustrated the seriousness of the current economic decline in Sweden, noting that GDP has currently declined 5% for 2009, but during Sweden's banking crisis of the early 1990's the greatest annual drop in GDP was only 2%. He said unemployment had been projected to peak in 2011, but was now expected to peak in 2010 since recent economic indicators were more encouraging. Still, he expected unemployment to be 11.5% by 2011.

#### Comment

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¶12. (SBU) The Ambassador will follow up with Finance Minister Borg regarding G-20 expectations when the two meet on August 26.

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